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Analysis of deferred tax by temporary differences:

(in millions of euros)	December 31, 2005	Impact on net income (loss)	Change in consolidated companies	Change and Other	December 31, 2006
Fair value adjustments of tax assets and liabilities resulting from business combinations	(8)	191	(2,496)	(5)	(2,318)
Provisions	371	(16)	240	(10)	585
Pension reserves	275	(243)	1,718	1	1,751
Prepaid pensions	(99)	141	(1,089)	(2)	(1,049)
Property, plant and equipment and intangible assets	216	(45)	(12)	(31)	128
Temporary differences arising from other balance sheet captions	289	(55)	471	(15)	690
Tax loss carry forwards and tax credits	5,836	127	4,691	(249)	10,405
Deferred tax assets, gross (liabilities)	**6,880**	**100**	**3,523**	**(311)**	**10,192**
Deferred tax assets not recognized	(5,274)	13	(5,975)	212	(11,024)
Net deferred tax assets (liabilities)	**1,606**	**113**	**(2,452)**	**(99)**	**(832)**
Of which directly included in shareholders' equity	(43)	7	–	–	(36)

Change during the period:

(in millions of euros)	December 31, 2005	Impact on net income (loss)	Translation adjustments	Change in consolidated companies	Other	December 31, 2006
Deferred tax assets recognized	1,768	(87)	(104)	108	7	1,692
Deferred tax liabilities	(162)	200	5	(2,560)	(7)	(2,524)
Net deferred tax assets (liabilities)	**1,606**	**113**	**(99)**	**(2,452)**	**–**	**(832)**

Deferred taxes not recognized relating to temporary differences on investments in subsidiaries, equity affiliates and joint ventures were zero at December 31, 2006 and December 31, 2005.

The dividend distribution proposed to the Annual Shareholders' Meeting (see Note 22) will have no tax consequences.

(d) Tax losses carried forward and temporary differences

Total tax losses carried forward represent a potential tax saving of €10,405 million at December 31, 2006 (€5,836 million at December 31, 2005). The potential tax savings relate to tax losses carried forward that expire as follows:

(in millions of euros)	Recognized	Unrecognized	Total
Years			
2007	3	199	202
2008	40	120	160
2009	27	66	93
2010	42	13	55
2011 and thereafter	1,327	8,568	9,895
TOTAL	**1,439**	**8,966**	**10,405**

In addition, temporary differences were €(213) million at December 31, 2006 (€1,044 million at December 31, 2005 and €1,115 million at December 31, 2004), of which €(2,271) million have been recognized and €2,058 million have not been recognized (€50 million and €994 million respectively at December 31, 2005 and €20 million and €1,095 million at December 31, 2004).

Recognized negative temporary differences mainly correspond to deferred tax liabilities that have been recorded resulting from Lucent purchase accounting entries (in particular intangible assets).

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Note 10 – Discontinued operations, assets held for sale and liabilities related to disposal groups held for sale

Discontinued operations for 2006, 2005 and 2004 are as follows:

- in 2006 and 2005: activities related to Alcatel's satellite subsidiaries, transport systems activities and critical systems integration activities not dedicated to operators or suppliers of telecommunications services to be disposed of or contributed to Thales. In addition, the initial capital gain (loss) on discontinued operations that were sold in 2004 was adjusted in 2006 and in 2005, due to ongoing legal proceedings related to these disposals and are also booked as income (loss) on discontinued operations;
- in 2004: disposal of Saft announced in October 2003 and finalized in January 2004, sale of the optical fiber activity announced in May 2004 and completed in July 2004, disposal of the mobile phones activity announced in April 2004 and completed in August 2004 and disposal of the electrical power systems activity (Saft Power Systems), announced in September 2004 and completed in January 2005; the net assets to be contributed to Thales as described above.

Other assets held for sale concern real estate property sales in progress at December 31, 2006, December 31, 2005 and December 31, 2004.

(in millions of euros)	Q4 2006	2006	2005	2004
Income statement:				
Income (loss) on discontinued operations	85	159	110	214

Income statements of discontinued operations for 2006, 2005 and 2004 in accordance with IFRSs are as follows:

Income statements of discontinued operations *(in millions of euros)*	Q4 2006	2006	2005	2004
Revenues	724	2,099	1,916	2,552
Cost of sales	(585)	(1,614)	(1,438)	(1,956)
Gross profit	**139**	**485**	**478**	**596**
Administrative and selling expenses	(66)	(230)	(213)	(291)
Research and development costs	(34)	(136)	(162)	(246)
Net capital gain (loss) on disposal of discontinued operations	(2)	15	(13)	211
Income (loss) from operating activities before restructuring costs, impairment of intangible assets and gain/(loss) on disposal of consolidated entities	**37**	**134**	**90**	**270**
Financial income (loss)	(3)	(13)	—	(34)
Other income (loss)[(1)]	51	38	20	(22)
Income (loss) from discontinued operations	**85**	**159**	**110**	**214**

(1) Including income tax expense.

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Balance sheet *(in millions of euros)*	December 31, 2006	December 31, 2005	December 31, 2004
Goodwill	795	—	—
Other assets	1,186	—	124
Cash	121	—	—
Assets of disposal groups	2,102	—	124
Other assets held for sale	15	50	72
Assets held for sale	**2,117**	**50**	**196**
Customers deposit and advances	(639)	—	—
Other liabilities	(967)	—	(97)
Liabilities related to disposal groups held for sale	**(1,606)**	**—**	**(97)**

The cash flows of discontinued operations for 2006, 2005 and 2004 in accordance with IFRSs are as follows:

(in millions of euros)	Q4 2006	2006	2005	2004
Net income (loss)	85	159	110	214
Net cash provided (used) by operating activities before changes in working capital	18	91	84	(50)
Other net increase (decrease) in net cash provided (used) by operating activities	289	81	136	(216)
Net cash provided (used) by operating activities (1)	307	172	220	(266)
Net cash provided (used) by investing activities (2)	(14)	(24)	10	299
Net cash provided (used) by financing activities (3)	(300)	(159)	(235)	(100)
TOTAL (1) + (2) + (3)	**(7)**	**(11)**	**(5)**	**(67)**

Note 11 – Earnings per Share

Basic earnings per share is computed using the number of shares issued, after deduction of the weighted average number of shares owned by consolidated subsidiaries and the weighting effect of shares issued during the year.

In accordance with IAS 33 revised (paragraph 23), the weighted average number of shares to be issued upon conversion of bonds redeemable for shares is included in the calculation of basic earnings per share.

Diluted earnings per share takes into account share equivalents having a dilutive effect, after deducting the weighted average number of share equivalents owned by consolidated subsidiaries, but not share equivalents that do not have a dilutive effect. Net income (loss) is adjusted for after–tax interest expense relating to convertible bonds.

The dilutive effects of stock option and stock purchase plans are calculated using the "treasury stock method", which provides that proceeds to be received from the exercise of options or purchase of stock are assumed to be used first to purchase shares at market price. The dilutive effects of convertible bonds and notes mandatorily redeemable for shares are calculated on the assumption that the bonds and notes will be systematically redeemed for shares (the "if converted method").

Regarding the Lucent acquisition, the entire issuance of Alcatel–Lucent shares is taken into account for the earnings per share calculation on a pro rata basis.

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The tables below reconcile basic earnings per share to diluted earnings per share for the six periods presented:

	Net income (loss) (in million of euros)	Number of shares	Per share amount
2006			
Basic earnings per share, attributable to the equity holders of the parent	(176)	1,449,000,656[1]	€(0.12)
Stock option plans	—	—	—
Convertible bonds	—	—	—
Diluted earnings per share, attributable to the equity holders of the parent	**(176)**	**1,449,000,656**	**€(0.12)**

(1) See Note 23a.

Ordinary shares:
Consolidated subsidiaries of the Group owned 58,466,525 Alcatel-Lucent ordinary shares (weighted average number) and no share equivalents.

Shares subject to future issuance:
The number of stock options not exercised as of December 31, 2006 amounted to 192,759,306 shares. These shares, subject to issuance in the future, have not been taken into account for the calculation of the diluted earnings per share, due to their anti-dilutive effect.
The following table summarizes the number of potential ordinary shares that were excluded from the diluted per share calculation, because the effect of including these potential shares was anti-dilutive:

Alcatel-Lucent's convertible bonds (OCEANE) issued on June 12, 2003	63,192,019
8% convertible securities (1)	3,067,982
7.75% convertible securities (1)	3,705,372
2.75% Series A convertible securities (1)	4,727,274
2.75% Series B convertible securities (1)	5,552,971

(1) Number of potential ordinary shares related to the convertible securities instrument derived from the Lucent acquisition are computed on a pro rata basis.

	Net income (loss) (in million of euros)	Number of shares	Per share amount
Q4 2006			
Basic earnings per share, attributable to the equity holders of the parent	(615)	1,678,022,630	€(0.37)
Stock option plans	—	—	—
Convertible bonds	—	—	—
Diluted earnings per share, attributable to the equity holders of the parent	**(615)**	**1,678,022,630**	**€(0.37)**

Ordinary shares:
Consolidated subsidiaries of the Group owned 58,610,566 Alcatel-Lucent ordinary shares (weighted average number) and no share equivalents.

Shares subject to future issuance:
The number of stock options not exercised as of December 31, 2006 amounted to 192,759,306 shares. These shares, subject to issuance in the future, have not been taken into account for the calculation of the diluted earnings per share, due to their anti-dilutive effect.

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The following table summarizes the number of potential ordinary shares that were excluded from the diluted per share calculation, because the effect of including these potential shares was anti-dilutive:

Alcatel-Lucent's convertible bonds (OCEANCE) issued on June 12, 2003	63,192,019
8% convertible securities[1]	12,271,928
7,75% convertible securities[1]	14,821,488
2,75% Series A convertible securities[1]	18,909,096
2,75% Series B convertible securities[1]	22,211,888

(1) Number of potential ordinary shares related to the convertible securities instrument derived from the Lucent acquisition are computed on a pro rata basis.

	Net income (loss) *(in million of euros)*	Number of shares	Per share amount
2005			
Basic earnings per share, attributable to the equity holders of the parent	930	1,367,994,653[1]	€0.68
Stock option plans	—	8,582,256	—
Convertible bonds	—	—	—
Diluted earnings per share, attributable to the equity holders of the parent	**930**	**1,376,576,909**	**€0.68**

(1) See Note 23a.

Ordinary shares:
Consolidated subsidiaries of the Group owned 59,323,183 Alcatel ordinary shares (weighted average number) and no share equivalents.

Shares subject to future issuance:
The number of stock options not exercised as of December 31, 2005 amounted to 149,359,801 shares. Only 8,582,256 share equivalents have been taken into account for the calculation of the diluted earnings per share, as the remaining share equivalents had an anti-dilutive effect.

Furthermore, 63,192,019 new or existing Alcatel ordinary shares, which are issuable in respect of Alcatel's convertible bonds (OCEANE) issued on June 12, 2003, have not been taken into account in the calculation of the diluted earnings per share amount due to their anti-dilutive effect.

	Net income (loss) *(in million of euros)*	Number of shares	Per share amount
Q4 2005			
Basic earnings per share, attributable to the equity holders of the parent	344	1,369,320,171	€ 0.25
Stock option plans	—	9,721,724	—
Convertible bonds	—	—	—
Diluted earnings per share, attributable to the equity holders of the parent	**344**	**1,379,041,895**	**€ 0.25**

Ordinary shares:
Consolidated subsidiaries of the Group owned 58,893,516 Alcatel-Lucent ordinary shares (weighted average number) and no share equivalents.

Shares subject to future issuance:
The number of stock options not exercised as of December 31, 2005 amounted to 149,359,801 shares. Only 9,721,724 share equivalents have been taken into account for the calculation of the diluted earnings per share, as the remaining share equivalents had an anti-dilutive effect.

Furthermore, 63,192,019 new or existing Alcatel-Lucent ordinary shares, which are issuable in respect of Alcatel's convertible bonds (OCEANE) issued on June 12, 2003, have not been taken into account in the calculation of the diluted earnings per share amount due to their anti-dilutive effect.

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	Net income (loss) *(in million of euros)*	Number of shares	Per share amount
2004			
Basic earnings per share, attributable to the equity holders of the parent	576	1,349,528,158[(1)]	€0.43
Stock option plans	—	12,849,283	—
Convertible bonds	—	—	—
Diluted earnings per share, attributable to the equity holders of the parent	**576**	**1,362,377,441**	**€0.42**

(1) See Note 23a.

Ordinary shares:
Consolidated subsidiaries of the Group owned 61,839,627 Alcatel ordinary shares (weighted average number) and no share equivalents.

Shares subject to future issuance:
The number of stock options not exercised as of December 31, 2004 amounted to 150,715,229 shares. Only 12,849,283 share equivalents have been taken into account for the calculation of the diluted earnings per share, as the remaining share equivalents had an anti-dilutive effect.

Furthermore, 63,192,019 new or existing Alcatel ordinary shares, which are issuable in respect of Alcatel's convertible bonds (OCEANE) issued on June 12, 2003, have not been taken into account in the calculation of the diluted earnings per share amount due to their anti-dilutive effect.

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Note 12 – Goodwill

(in millions of euros)	Net
Goodwill at January 1, 2004	**3,630**
Additions	214
Disposals and discontinued operations	(7)
Impairment losses for the period	(1)
Net effect of exchange rate changes	(59)
Other changes	(3)
Goodwill at December 31, 2004	**3,774**
Additions	173
Disposals and discontinued operations	(300)
Changes during goodwill allocation period	3
Impairment losses for the period	—
Net effect of exchange rate changes	123
Other changes	(1)
Goodwill at December 31, 2005	**3,772**
Additions	8,091
Disposals and discontinued operations	(795)
Changes during goodwill allocation period	(15)
Impairment losses for the period	—
Net effect of exchange rate changes	(71)
Other changes	(5)
Goodwill at December 31, 2006	**10,977**

Main changes accounted for in 2006:

Additions to goodwill recorded in 2006 relate primarily to the merger with Lucent (see Note 3).

Reduction in goodwill presented in the caption "Disposals and discontinued operations" concerns the goodwill related to the businesses to be disposed of or contributed to Thales (see Note 3).

Main changes accounted for in 2005:

Additions to goodwill recorded in 2005 relate primarily to the acquisitions of Native Networks and the industrial activities (Alenia Spazio) and service activities (Telespazio) of Finmeccanica (see Note 3).

Reduction in goodwill presented in the caption "disposals and discontinued operations" relates to the proportionate consolidation of the satellite industrial activity goodwill (fully consolidated in 2004 but consolidated at 67% in 2005) (see Note 3).

Goodwill allocation:

All goodwill recognized in 2006, 2005 and 2004 has been allocated to the cash generating units by the accounting year–ends concerned, however, the allocation of the goodwill generated by the Lucent acquisition has not yet been finalized.

The goodwill amounts relating to business combinations, for which the initial accounting period has not yet been completed at December 31, 2006, are preliminary.

Impairment tests:

One impairment test of goodwill was carried out at the IFRS transition date. This impairment test did not lead to the recording of any impairment losses.

An additional impairment test was carried out at December 31, 2005 on the SSD business division (Space Solutions Division), as a result of the business combination that occurred during the year (see Note 3). The test did not lead to the recording of any impairment losses.

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The 2006 annual impairment tests of goodwill (performed in May/June 2006 on the basis of published data at March 31, 2006) did not result in the recognition of any impairment losses in 2006.

The additional impairment test of goodwill performed in December 2006 (on Alcatel's goodwill excluding Lucent's and Nortel's goodwill) due to the reorganization of the reporting structure did not result in the recognition of any impairment losses in 2006.

In those group of cash generating units ("CGU" – please refer to Note 1g) in which there is significant goodwill, the data and assumptions used for the goodwill impairment tests were as follows:

2006 Test	Net carrying amount of goodwill	Difference between recoverable amount and the carrying amount of the net assets	Discount rate	Valuation method
OND CGU (optical Network division)	1,176	718	9.5%	Discounted cash flows and other data(2)
MCD CGU (multicore division)	203	243	9.5%	Same as above(2)
Other CGU(1)	9,598			Same as above(2)
Total net	**10,977**			

(1) Including the goodwill from the Lucent acquisition for €8,066 million at December 31, 2006, which has not been allocated so far.

(2) Future cash flows for 5 years and disposal value. Other data: market capitalizations and transactions. Growth rates are those used in the Group's budgets and industry rates for the subsequent periods. Perpetual growth rates used for the residual values are between 0% and 4% depending on the CGU.

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Note 13 – Intangible assets

(a) Gross value

(in millions of euros)	Capitalized development costs	Other intangible assets	Total
At January 1, 2004	**828**	**342**	**1,170**
Capitalization	326		326
Additions	—	27	27
Assets held for sale, discontinued operations and disposals	(4)	(18)	(22)
Business combinations	—	80	80
Net effect of exchange rate changes	(8)	(20)	(28)
Other changes	(120)	43	(77)
At December 31, 2004	**1,022**	**454**	**1,476**
Capitalization	349	—	349
Additions	—	27	27
Assets held for sale, discontinued operations and disposals	(67)	(22)	(89)
Business combinations	—	24	24
Net effect of exchange rate changes	23	37	60
Other changes	(48)	(32)	(80)
At December 31, 2005	**1,279**	**488**	**1,767**
Capitalization	386	—	386
Additions	—	16	16
Assets held for sale, discontinued operations and disposals	(66)	(31)	(97)
Write–offs[1]	(522)	(234)	(756)
Business combinations[2]	—	5,062	5,062
Net effect of exchange rate changes	(24)	(14)	(38)
Other changes	165	(7)	158
At December 31, 2006	**1,218**	**5,280**	**6,498**

(1) Mainly related to discontinued product lines (refer to Notes 3 and 27c).
(2) Mainly related to Lucent acquisition (refer to Note 3).

Other intangible assets include primarily intangible assets acquired in business combinations (acquired technologies, in process research and development and customer relationships), patents and licenses.

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(b) Amortization and impairment losses

(in millions of euros)

	Capitalized development costs	Other intangible assets	Total
At January 1, 2004	**(290)**	**(297)**	**(587)**
Amortization	(196)	(32)	(228)
Impairment losses for the period	(88)	(18)	(106)
Reversals of impairment losses	—	—	—
Assets held for sale, discontinued operations and disposals	4	18	22
Net effect of exchange rate changes	5	12	17
Other changes	119	(8)	111
At December 31, 2004	**(446)**	**(325)**	**(771)**
Amortization	(248)	(49)	(297)
Impairment losses	—	(3)	(3)
Reversals of impairment losses	—	—	—
Assets held for sale, discontinued operations and disposals	54	21	75
Net effect of exchange rate changes	(9)	(24)	(33)
Other changes	50	31	81
At December 31, 2005	**(599)**	**(349)**	**(948)**
Amortization	(277)	(104)	(381)
Impairment losses	(104)	(40)	(144)
Write-offs[(1)]	325	1	326
Reversals of impairment losses	—	—	—
Assets held for sale, discontinued operations and disposals	37	25	62
Net effect of exchange rate changes	11	20	31
Other changes	(110)	13	(97)
At December 31, 2006	**(717)**	**(434)**	**(1,151)**

(1) Mainly related to discontinued product lines (refer to Notes 3 and 27c).

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(c) Net value

(in millions of euros)

	Capitalized development costs	Other intangible assets	Total
At January 1, 2004	**538**	**45**	**583**
Capitalization	326	—	326
Additions	—	27	27
Amortization	(196)	(32)	(228)
Impairment losses for the period	(88)	(18)	(106)
Reversals of impairment losses	—	—	—
Assets held for sale, discontinued operations and disposals	—	—	—
Business combinations	—	80	80
Net effect of exchange rate changes	(3)	(8)	(11)
Other changes	(1)	35	34
At December 31, 2004	**576**	**129**	**705**
Capitalization	349	—	349
Additions	—	27	27
Amortization	(248)	(49)	(297)
Impairment losses for the period	—	(3)	(3)
Reversals of impairment losses	—	—	—
Assets held for sale, discontinued operations and disposals	(13)	(1)	(14)
Business combinations	—	24	24
Net effect of exchange rate changes	14	13	27
Other changes	2	(1)	1
At December 31, 2005	**680**	**139**	**819**
Capitalization	386	—	386
Additions	—	16	16
Amortization	(277)	(104)	(381)
Impairment losses	(104)	(40)	(144)
Write offs(1)	(197)	(233)	(430)
Reversals of impairment losses	—	—	—
Assets held for sale, discontinued operations and disposals	(29)	(6)	(35)
Business combinations(2)	—	5,062	5,062
Net effect of exchange rate changes	(13)	6	(7)
Other changes	55	6	61
At December 31, 2006	**501**	**4,846**	**5,347**

(1) Mainly related to discontinued product lines (refer to Notes 3 and 27c).
(2) Mainly related to Lucent acquisition (refer to Note 3).

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Note 14 – Property, plant and equipment

(a) Changes in property, plant and equipment, gross

(in millions of euros)	Land	Buildings	Plant, equipment and tools	Other	Total
At January 1, 2004	**148**	**1,634**	**3,533**	**777**	**6,092**
Additions	—	12	134	80	226
Assets held for sale, discontinued operations and disposals	(60)	(481)	(1,003)	(125)	(1,669)
Business combinations	—	—	3	—	3
Net effect of exchange rate changes	(1)	(26)	(79)	(3)	(109)
Reclassifications and other changes	(6)	59	156	(81)	128
At December 31, 2004	**81**	**1,198**	**2,744**	**648**	**4,671**
Additions	3	12	152	95	262
Assets held for sale, discontinued operations and disposals	(13)	(255)	(522)	(76)	(866)
Business combinations	9	69	42	8	128
Net effect of exchange rate changes	4	56	171	10	241
Reclassifications and other changes	1	(48)	100	(72)	(19)
At December 31, 2005	**85**	**1,032**	**2,687**	**613**	**4,417**
Additions	1	28	153	100	282
Assets held for sale, discontinued operations and disposals (1)	(38)	(364)	(307)	(120)	(829)
Write offs	—	(17)	(36)	(16)	(69)
Business combinations (2)	245	622	302	50	1,219
Net effect of exchange rate changes	(2)	(33)	(95)	(8)	(138)
Other changes	2	(7)	44	(47)	(8)
At December 31, 2006	**293**	**1,261**	**2,748**	**572**	**4,874**

(1) Related to activities to be disposed of or contributed to Thales (refer to Note 3).
(2) Mainly related to Lucent acquisition (refer to Note 3).

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(b) Changes in accumulated depreciation of property, plant and equipment and impairment losses

(in millions of euros)

	Land	Buildings	Plant, equipment and tools	Other	Total
At January 1, 2004	**(21)**	**(1,016)**	**(2,988)**	**(631)**	**(4,656)**
Depreciation charge	(1)	(69)	(207)	(40)	(317)
Impairment losses	(3)	(2)	(5)	—	(10)
Assets held for sale, discontinued operations and disposals	14	347	930	102	1,393
Net effect of exchange rate changes	—	12	67	2	81
Reclassifications and other changes	(1)	13	(123)	44	(67)
At December 31, 2004	**(12)**	**(715)**	**(2,326)**	**(523)**	**(3,576)**
Depreciation charge	(1)	(55)	(193)	(35)	(284)
Impairment losses	—	(1)	—	—	(1)
Assets held for sale, discontinued operations and disposals	1	176	463	64	704
Net effect of exchange rate changes	—	(25)	(143)	(7)	(175)
Reclassifications and other changes	(2)	65	(50)	13	26
At December 31, 2005	**(14)**	**(555)**	**(2,249)**	**(488)**	**(3,306)**
Depreciation charge	—	(49)	(177)	(24)	(250)
Impairment losses	—	—	—	(2)	(2)
Reversals of impairment losses	—	—	—	—	
Write offs	—	17	36	16	69
Assets held for sale, discontinued operations and disposals[1]	3	203	231	89	526
Net effect of exchange rate changes	—	15	82	7	104
Other changes	3	(7)	15	—	11
At December 31, 2006	**(8)**	**(376)**	**(2,062)**	**(402)**	**(2,848)**

(1) Related to activities to be disposed of or contributed to Thales (refer to Note 3).

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(c) Changes in property, plant and equipment, net

(in millions of euros)	Land	Buildings	Plant, equipment and tools	Other	Total
At January 1, 2004	**127**	**618**	**545**	**146**	**1,436**
Additions	—	12	134	80	226
Depreciation charge	(1)	(69)	(207)	(40)	(317)
Impairment losses	(3)	(2)	(5)	—	(10)
Assets held for sale, discontinued operations and disposals	(46)	(134)	(73)	(23)	(276)
Business combinations	—	—	3	—	3
Net effect of exchange rate changes	(1)	(14)	(12)	(1)	(28)
Reclassifications and other changes	(7)	72	33	(37)	61
At December 31, 2004	**69**	**483**	**418**	**125**	**1,095**
Additions	3	12	152	95	262
Depreciation charge	(1)	(55)	(193)	(35)	(284)
Impairment losses	—	(1)	—	—	(1)
Assets held for sale, discontinued operations and disposals	(12)	(79)	(59)	(12)	(162)
Business combinations	9	69	42	8	128
Net effect of exchange rate changes	4	31	28	3	66
Reclassifications and other changes	(1)	17	50	(59)	7
At December 31, 2005	**71**	**477**	**438**	**125**	**1,111**
Additions	1	28	153	100	282
Depreciation charge	—	(49)	(177)	(24)	(250)
Impairment losses	—	—	—	(2)	(2)
Reversals of impairment losses	—	—	—	—	—
Assets held for sale, discontinued operations and disposals[1]	(35)	(161)	(76)	(31)	(303)
Business combinations[2]	245	622	302	50	1,219
Net effect of exchange rate changes	(2)	(18)	(13)	(1)	(34)
Other changes	5	(14)	59	(47)	4
At December 31, 2006	**285**	**885**	**686**	**170**	**2,026**

(1) Related to activities to be disposed of or contributed to Thales (refer to Note 3).
(2) Mainly related to Lucent acquisition (refer to Note 3).

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Note 15 – Finance leases and operating leases

(a) Finance leases (IFRS)

Property, plant and equipment held under finance leases have a net carrying amount of €45 million at December 31, 2006 (€54 million at December 31, 2005 and €49 million at December 31, 2004). Such finance leases relate primarily to plant and equipment.

Future minimum lease payments under non-cancelable finance leases are shown in Note 31a — Off balance sheet commitments.

The main finance lease contract concerns a company consolidated proportionately at 51%, Alda Marine, which leases four vessels as part of its activity of laying and maintaining submarine cables. The net carrying amount of these vessels recognized in property, plant and equipment was €45 million at December 31, 2006. The corresponding obligation to pay future lease payments was €51 million at December 31, 2006.

(b) Operating leases

Future minimum lease payments under non-cancelable operating leases are shown in Note 31a — Off balance sheet commitments.

Future minimum sublease payments expected to be received under non-cancelable operating subleases were €202 million at December 31, 2006 (€27 million at December 31, 2005 and €7 million at December 31, 2004).

Lease payments under operating leases recognized as an expense in the income statement are analyzed as follows:

(in millions of euros)	2006	2005	2004
Lease payments — minimum	121	97	49
Lease payments — conditional	37	42	61
Sublease rental income	(14)	(10)	(5)
Total recognized in the income statement	**144**	**129**	**105**

Note 16 – Share in net assets of equity affiliates and joint ventures

(a) Share in net assets of equity affiliates

	Percentage owned			Value *(in millions of euros)*		
	2006	2005	2004	2006	2005	2004
Thales(1)	9.5%	9.5%	9.5%	372	334	288
Draka Comteq BV(2)	49.9%	49.9%	49.9%	117	127	132
TAMP(3)	—	—	45.0%	—	—	33
2Wire(4)	27.5%			82	—	—
Other (less than €50 million)	—	—	—	111	145	151
Share in net assets of equity affiliates				**682**	**606**	**604**

(1) Although Alcatel-Lucent only has a 9.5% stake in Thales, Alcatel-Lucent is nevertheless the largest private shareholder of this group, with three seats on Thales' Board of Directors. Due to the Group's continuing significant influence on this company, Alcatel-Lucent still accounts for Thales using the equity method. At December 31, 2006, Alcatel-Lucent's stake was 9.5% (12.8% in voting rights). Following the contribution of some assets to Thales in January 2007, Alcatel-Lucent's stake in Thales is now 20.95%. The Group's share of net income (loss) accounted for during 2006 corresponds to Thales' results for the second half of 2005, the first half of 2006 and an estimation of the second half of 2006.

(2) Under the agreement, dated July 2, 2004, between Alcatel and Draka Holding BV concerning the business combination of the optical fiber and communication cable activities of the two groups, a new company Draka Comteq BV was created. Alcatel-Lucent owns 49.9% of this new company, which is consolidated under the equity method beginning July 1, 2004 (see Note 3).

(3) Under the agreement, dated August 31, 2004, between Alcatel and TCL Communication Technology Holdings Limited concerning the creation of a new joint venture for mobile handsets, a new company, TAMP, was created. Alcatel owned 45% of this company, which was consolidated under the equity method from September 1, 2004 to July 18, 2005, when Alcatel swapped its 45% stake in the joint venture for shares in TCL Communication Holding Ltd, representing 4.8% of this listed company in which the Group has no significant influence (see Note 3).

(4) During the first quarter of 2006, Alcatel acquired a 27.5% stake in 2Wire (see Note 3).

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Alcatel–Lucent's share in the market capitalization of listed equity affiliates at December 31 is as follows:

(in millions of euros)	2006	2005	2004
Thales	615	624	575

(b) Change in share of net assets of equity affiliates

(in millions of euros)	2006	2005	2004
Carrying amount at January 1	**606**	**604**	**501**
Change in equity affiliates	82	(16)	195
Share of net income (loss)(1)	22	(14)	(61)
Net effect of exchange rate changes	(15)	28	(11)
Other changes	(13)	4	(20)
Carrying amount at December 31	**682**	**606**	**604**

(1) Including €8 million and €30 million of impairment losses respectively in 2006 and 2004 relating to equity affiliate goodwill (see Note 7).

(c) Summarized financial information for equity affiliates

Summarized financial information for Thales:

(in millions of euros)	December 31, 2006(1)	December 31, 2005(1)	January 1, 2005(2)	December 31, 2004
Balance sheet				
Non-current assets	4,164	4,271	4,228	4,239
Current assets	10,858	9,616	9,390	9,262
Total assets	**15,022**	**13,887**	**13,618**	**13,501**
Shareholders' equity	2,294	2,103	1,741	1,601
Non-current liabilities	2,720	2,583	2,555	2,553
Current liabilities	10,008	9,201	9,322	9,346
Total liabilities	**15,022**	**13,887**	**13,618**	**13,501**
Income statement				
Revenues	10,264	10,263	—	10,283
Income (loss) from operating activities	576	549	—	571
Net income (loss) attributable to equity holders of the parent	388	334	—	326

(1) In view of the timing of the publication of Thales' financial statements, and as this equity affiliate is listed on a securities exchange, the Group cannot provide any non-published information between two publication dates that may have been obtained by the directors representing Alcatel-Lucent on the Thales Board of Directors, due to the rules of communication applicable to listed companies.

(2) The accounting options made by Thales governing the first-time adoption of IFRSs are similar to those made by Alcatel-Lucent, except for the timing of the first application of the standards, IAS 32 and 39, relating to financial instruments (Alcatel-Lucent first applied these at January 1, 2004 and Thales at January 1, 2005). As it is not possible to restate the 2004 accounts of Thales for the impact of the application of these standards, Alcatel-Lucent's share of the change in shareholders' equity resulting from this first application has been recognized in 2005 in "net income (loss) changes recognized directly in equity".

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Aggregated financial information for other equity affiliates as if those entities were fully consolidated:

(in millions of euros)	2006	2005	2004
Total assets	1,389	1,195	1,248
Liabilities (excluding shareholders' equity)	699	563	573
Shareholders' equity	690	632	675
Revenues	1,148	1,146	712
Net income (loss) attributable to equity holders of the parent	(59)	(68)	(96)

(d) Aggregated financial information for joint ventures

Aggregated financial information for the Group's share in the net assets of joint ventures proportionately consolidated (Alcatel Alenia Space, Telespazio, Evolium and Alda Marine in 2006 and 2005 and Alda Marine and Evolium in 2004) are as follows:

(in millions of euros)	2006	2005	2004
Balance sheet data			
Non-current assets[1]	57	1,314	209
Current assets[1]	1,723	773	6
Shareholders' equity	776	983	90
Other non-current liabilities[1]	—	135	47
Current liabilities[1]	1,004	969	78
Income statement data			
Revenues	—	2	9
Cost of sales	28	79	65
Income (loss) from operating activities before restructuring, impairment of intangible assets and capital gain on disposal of consolidated entities	21	3	(1)
Income (loss) from discontinued operations[2]	39	47	—
Net income (loss) attributable to equity holders of the parent	56	44	(5)
Cash flow statement data			
Net cash provided (used) by operating activities	28	51	60
Net cash provided (used) by investing activities	(26)	(60)	(53)
Net cash provided (used) by financing activities	(3)	9	(9)
Net cash provided (used) by operating activities of discontinued operations[2]	134	29	—
Net cash provided (used) by investing activities of discontinued operations[2]	(26)	(2)	—
Net cash provided (used) by financing activities of discontinued operations[2]	(110)	2	—

(1) Aggregated financial information for Alcatel Alenia Space and Telespazio for 2006 are reported as assets held for sale (included in current assets) and liabilities related to disposal groups held for sale (included in current liabilities) (see Notes 3 and 10).

(2) Aggregated financial information for Alcatel Alenia Space and Telespazio only relates to six months of activity in 2005 and full year 2006 and has been reported as discontinued operations (see Note 3 and Note 10).

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Note 17 – Financial assets

(In millions of euros)	2006			2005			2004		
	Other non-current financial assets[1]	Marketable securities[2]	Total	Other non-current financial assets	Marketable securities	Total	Other non-current financial assets	Marketable securities	Total
Financial assets available for sale[3]	674	1,122	1,796	122	—	122	213	105	318
Financial assets at fair value through profit or loss		820	820		640	640		447	447
Financial assets at amortized cost	129	—	129	184		184	341		341
TOTAL	**803**	**1,942**	**2,745**	**306**	**640**	**946**	**554**	**552**	**1,106**

(1) Of which €296 million matures within one year.
(2) Of which €697 million is non-current and €1,245 million is current as of December 31, 2006.
(3) The change in other non-current financial assets available for sale between 2005 and 2006 is mainly due to Lucent's restricted cash (of which €239 million in connection with the Winstar litigation – refer to Note 34).

No financial asset is considered as being held to maturity.

(a) Financial assets available for sale

(In millions of euros)	2006			2005			2004		
	Other non-current financial assets	Marketable securities	Total	Other non-current financial assets	Marketable securities	Total	Other non-current financial assets	Marketable securities	Total
Net carrying amount at January 1	**122**	**—**	**122**	**213**	**105**	**318**	**215**	**92**	**307**
Additions / (disposals)	18	(556)	(538)	(4)	(49)	(53)	23	5	28
Fair value changes	26	10	36	(13)	(56)	(69)	23	8	31
Impairment losses[1]	(4)	—	(4)	(47)	—	(47)	(44)	—	(44)
Change in consolidated scope	448	1,423	1,871	—	—	—	—	—	—
Other changes[2]	64	245	309	(27)	—	(27)	(4)	—	(4)
Net carrying amount at December 31	**674**	**1,122**	**1,796**	**122**	**—**	**122**	**213**	**105**	**318**
Of which: – at fair value	*54*	*1,115*	*1,169*	*36*	—	*36*	*70*	*105*	*175*
– at cost	*620*	*7*	*627*	*86*	—	*86*	*143*	—	*143*

(1) See Note 7 – of which €23 million in 2005 relates to the Avanex shares due to an unfavorable change in the market price.
(2) Of which €232 million is reclassified from marketable securities at fair value through profit and loss to marketable securities available for sale category due to the amendment of IAS 39 related to the fair value option (see Note 1u).

Financial assets available for sale are stated at fair value, except for non-listed financial assets, which are stated at cost, if no reliable fair value exists.

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(in millions of euros)	2006	2005	2004
Fair value changes			
Fair value changes recognized directly in shareholders' equity	36	(13)	32
Changes resulting from gains (losses) previously recognized in shareholders' equity now recognized in net income (loss) due to disposals[1]	—	(56)	—

(1) Relates to the sale of the Nexans shares during the first quarter of 2005 (see Note 8).

(b) Financial assets at fait value through profit or loss

(in millions of euros)	2006	2005	2004
Net carrying amount at January 1	**640**	**447**	**174**
Additions / (disposals)	431	148	264
Fair value changes	2	19	6
Impairment losses	—	—	—
Other changes[1]	(253)	26	3
Net carrying amount at December 31	**820**	**640**	**447**

(1) Of which €232 million is reclassified to marketable securities available for sale due to the amendment of IAS 39 related to the fair value option (see Note 1u).

(c) Financial assets at amortized cost

(in millions of euros)	2006	2005	2004
Net carrying amount at January 1	**184**	**341**	**829**
Additions / (disposals)	(44)	(94)	(569)
Impairment losses[1]	—	25	74
Change in consolidation scope	(9)	—	—
Other changes (reclassifications)	(2)	(88)	7
Net carrying amount at December 31	**129**	**184**	**341**

(1) See Note 7.

Note 18 – Operating working capital

(in millions of euros)	December 31, 2006	December 31, 2005	December 31, 2004
Inventories and work in progress, net	2,259	1,438	1,273
Trade receivables and related accounts, net	3,877	3,420	2,693
Advances and progress payments	87	124	90
Customers' deposits and advances	(778)	(1,144)	(973)
Trade payables and related accounts	(4,022)	(3,755)	(3,350)
Amounts due from customers on construction contracts	615	917	729
Amounts due to customers on construction contracts	(273)	(138)	(133)
Currency derivatives on working capital – other assets	-	-	102
Operating working capital, net	**1,765**	**862**	**431**

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Analysis of amounts due from/to customers on construction contracts *(in millions of euros)*	December 31, 2006	December 31, 2005	December 31, 2004
Amounts due from customers on construction contracts	615	917	729
Amounts due to customers on construction contracts	(273)	(138)	(133)
TOTAL	**342**	**779**	**596**
Work in progress on construction contracts, gross	137	281	291
Work in progress on construction contracts, depreciation	(23)	(29)	(30)
Customer receivables on construction contracts	299	700	606
Product sales reserves – construction contracts	(71)	(173)	(271)
TOTAL	**342**	**779**	**596**

(in millions of euros)	December 31, 2005	Cash flow	Change in consolidated companies	Translation adjustments and other	December 31, 2006[5]
Inventories and work in progress[2] & [3]	2,113	116	769	(247)	2,751
Trade receivables and related accounts[2]	4,348	137	68	(186)	4,367
Advances and progress payments	124	5	(49)	7	87
Customers' deposits and advances[4]	(1,144)	100	262	4	(778)
Trade payables and related accounts	(3,755)	(229)	(180)	142	(4,022)
Operating working capital, gross	**1,686**	**129**	**870**	**(280)**	**2,405**
Product sales reserves – construction contracts[1]	(173)	–	69	34	(70)
Valuation allowances	(651)	–	67	14	(570)
Operating working capital, net	**862**	**129**	**1,006**	**(232)**	**1,765**

(1) Including mainly acquisition of Lucent (representing €793 million) and reclassification of assets and liabilities of discontinued activities on specific line items of the balance sheet. Please refer to Notes 3 and 10.
(2) Including amounts relating to construction contracts presented in the balance sheet caption "amounts due from/to customers on construction contracts".
(3) Of which €429 million in the column "change in consolidated companies" related to the step-up of inventories accounted for in the purchase accounting of Lucent as described in Note 3. Amounts related to the step-up of inventories included in the columns "translation adjustments and other" and "December 31, 2006" are respectively €167 million and €263 million.
(4) Of which €639 million included in the column "change in consolidated companies" related to the reclassification to liabilities related to disposal groups held for sale of customers' advances in discontinued activities.
(5) Of which €783 million of closing operating working capital net in Lucent.

Receivables sold without recourse

Balances *(in millions of euros)*	December 31, 2006	December 31, 2005	December 31, 2004
Receivables sold without recourse[1]	978	999	841

(1) See accounting policies in Note 1s.

Changes in receivables sold without recourse *(in millions of euros)*	Q4 2006	2006	2005	2004
Impact on cash flows from operating activities	85	(21)	158	(57)

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Note 19 – Inventories and work in progress

(a) Analysis of net value

(in millions of euros)	2006	2005	2004
Raw materials and goods	542	467	501
Work in progress excluding construction contracts	752	712	592
Finished products	1,320	653	645
Gross value (excluding construction contracts)	**2,614**	**1,832**	**1,738**
Valuation allowance	(355)	(394)	(465)
Net value (excluding construction contracts)	**2,259**	**1,438**	**1,273**
Work in progress on construction contracts, gross[1]	137	281	291
Valuation allowance[1]	(23)	(29)	(30)
Work in progress on construction contracts, net	**114**	**252**	**261**
Total, net	**2,373**	**1,690**	**1,534**

(1) Included in the amounts due from/to customers on construction contracts.

(b) Change in valuation allowance

(in millions of euros)	2006	2005	2004
At January 1	**(423)**	**(495)**	**(978)**
(Additions) / reversals	(77)	(18)	20
Utilization	54	131	427
Changes in consolidation group	54	11	40
Net effect of exchange rate changes and other changes	14	(52)	(4)
At December 31	**(378)**	**(423)**	**(495)**

Note 20 – Trade receivables and related accounts

(in millions of euros)	2006	2005	2004
Receivables bearing interest	296	138	101
Other trade receivables	3,773	3,510	2,876
Gross value – (excluding construction contracts)	**4,069**	**3,648**	**2,977**
Valuation allowance	(192)	(228)	(284)
Net value – (excluding construction contracts)	**3,877**	**3,420**	**2,693**
Receivables on construction contracts[1]	299	700	606
Total, net	**4,176**	**4,120**	**3,299**
Of which due after one year on the "Net value – (excluding construction contracts)"[2]	*34*	*–*	*–*

(1) Included in the amounts due from/to customers on construction contracts.
(2) Data is not available for 2004.

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Note 21 – Other assets and liabilities

(in millions of euros)	December 31, 2006	December 31, 2005	December 31, 2004
Other assets			
Other current assets	1,006	827	1,418
Other non–current assets	203	468	332
TOTAL	**1,209**	**1,295**	**1,750**
Of which:			
Currency derivatives on working capital	–	–	102
Other currency derivatives	101	105	420
Interest–rate derivatives	36	178	148
Other current and non–current assets	1,072	1,012	1,080
Other liabilities			
Other current liabilities	1,938	1,931	2,157
Other non–current liabilities	303	295	201
TOTAL	**2,241**	**2,226**	**2,358**
Of which: Currency derivatives on working capital	–	–	–
Other currency derivatives	71	128	360
Interest–rate derivatives	10	71	43
Other current and non–current liabilities	2,160	2,027	1,955

Note 22 – Allocation of 2006 net income

The Board of Directors will propose to the Shareholders' Ordinary Annual General Meeting to distribute a dividend of €0.16 per share in the aggregate amount of €370 million for the year ended December 31, 2006 (distributions in previous years: a dividend of €0.16 per share in the aggregate amount of €229 million was distributed for 2005 and no dividend was distributed for 2004).

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Note 23 – Shareholders' equity

(a) Number of shares comprising the capital stock

December 31, 2006	Number of shares
Number of ordinary shares issued (share capital)	2,309,679,141
Treasury shares	(58,739,991)
Number of shares in circulation	**2,250,939,150**
Weighting effect of share issues for stock options exercised	(512,996)
Weighting effect of treasury shares	(273,466)
Weighting effect of share issues due to the combination with Lucent	(801,152,032)
Weighting effect of share issues in respect of business combinations	–
Number of shares used for calculating basic earnings per share	**1,449,000,656**

December 31, 2005	Number of shares
Number of ordinary shares issued (share capital)	1,428,541,640
Treasury shares	(58,920,710)
Number of shares in circulation	**1,369,620,930**
Weighting effect of share issues for stock options exercised	(1,223,804)
Weighting effect of treasury shares	(402,473)
Weighting effect of share issues in respect of business combinations	–
Number of shares used for calculating basic earnings per share	**1,367,994,653**

December 31, 2004	Number of shares
Number of ordinary shares issued (share capital)	1,305,455,461
Number of notes mandatorily redeemable for new or existing shares	120,780,519
Treasury shares	(60,262,153)
Number of shares in circulation	**1,365,973,827**
Weighting effect of share issues for stock options exercised	(1,664,706)
Weighting effect of treasury shares	(1,577,474)
Weighting effect of share issues in respect of business combinations	(13,203,489)
Number of shares used for calculating basic earnings per share	**1,349,528,158**

(b) Capital increase program for employees with subscription stock option plan

Under a capital increase program for employees of the Group, approved by the Board of Directors on March 7, 2001, 91,926 Class A shares were issued at a price of €50 per share (all Class A shares are now referred to as ordinary shares). Each share subscribed included the right to receive three options, each exercisable for one Class A share. 275,778 options were granted and are exercisable during the one–year period from July 1, 2004 until July 1, 2005 or from the end of the unavailability period set by article 163 bis C of the General Tax Code (4 years on this date), for the beneficiaries who were employees of a member of the Group whose registered office is located in France at the time the options were granted.

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(c) Capital stock and additional paid–in capital

At December 31, 2006, the capital stock consisted of 2,309,679,141 ordinary shares of nominal value €2 (1,428,541,640 ordinary shares of nominal value €2 at December 31, 2005 and 1,305,455,461 ordinary shares of nominal value €2 at December 31, 2004).

During 2006, increases in capital stock and additional paid–in capital amounted to €8,942 million. These increases related to the following actions:

- issuance of 878,139,615 shares related to the combination with Lucent merger for €8,922 million (including additional paid–in capital of €7,166 million);
- issuance of 2,697,886 shares for €20 million, as a result of the exercise of 2,697,886 options (including additional paid–in capital of €11 million);
- redemption of 300,000 bonds redeemable for Alcatel–Lucent shares in connection with the acquisition of Spatial Wireless in 2004, generating a capital increase of €3 million (including additional paid–in capital of €3 million).

During 2005, increases in capital stock and additional paid–in capital amounted to €662.1 million. These increases related to the following actions:

- issuance of 1,855,913 shares for €12 million, as a result of the exercise of 1,855,913 options (including additional paid–in capital of €8.3 million);
- redemption of 450,000 bonds redeemable for Alcatel shares in connection with the acquisition of Imagic TV in 2003 and Spatial Wireless in 2004 generating a capital increase of €5.1 million (including additional paid–in capital of €4.2 million);
- redemption of 120,780,266 ORANE notes issued in 2002 and redeemable for new or existing Alcatel shares, generating a capital increase of €645.0 million, including additional paid–in capital of €403.4 million.

During 2004, increases in capital stock and additional paid–in capital amounted to €238 million. These increases related to the following actions:

- issuance of 1,508,728 shares for €9.9 million, as a result of the exercise of 1,508,728 options (including additional paid–in capital of €6.9 million);
- redemption of 3,212 ORANE notes issued in 2002 and redeemable for new or existing Alcatel shares, generating a capital increase of €0.017 million, including additional paid–in capital of €0.011 million;
- acquisition of Spatial Wireless in December 2004, which resulted in the issuance of 17,390,262 shares for €207.2 million (including additional paid–in capital of €172.4 million); in addition, of the 1,598,072 bonds redeemable for Alcatel shares issued in this transaction by Coralec (a subsidiary of Alcatel) at the price of €11.912 to cover the exercise of options and warrants, 393,035 bonds were redeemed by the issuance of an equal number of Alcatel shares, generating a capital increase of €4.7 million, including additional paid–in capital of €3.9 million; and
- redemption of 300,000, 400,000, 50,000 and 1,000,000 bonds redeemable for Alcatel shares to cover option exercises, warrant exercises and note conversions issued in connection with the acquisitions of Astral Point in 2002, Telera in 2002, Imagic TV in 2003 and TiMetra in 2003, generating capital increases of €4.9 million, €2.1 million, €0.4 million and €8.1 million, including additional paid–in capital of €4.3 million, €1.3 million, €0.3 million and €6.1 million, respectively.